

GASB Threatens to Reinforce Bad Government Accounting Practices

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The Stakes are High

Schools. Roads. Public Safety. Taxes. Social Services. What comes to mind when you think about your local and state governments and their responsibility to serve you? These are the issues on which politicians campaign. They're the issues that make headlines. They're the issues that matter to all of us in our daily lives—and when we hold our leaders accountable at the ballot box.

We elect our mayors, governors and lawmakers based on their promises. Once they are in office, the primary vehicle for keeping those promises is the budget. Looking past the pages of complex figures and accounting jargon, a budget is simply a statement of priorities. It's a plan to take limited resources and use them in a way that best serves the public's needs. By law, 49 of the 50 states must balance their budgets, at least in theory. Governments should balance the money they collect and the money they spend.

But, what happens when budgets aren't based on reality? If we can't trust the numbers, how can our elected leaders make good decisions? How can we have faith in what they're telling us?

Unfortunately, far too many municipal and state budgets across the nation are fantasy and illusion—not reality. Our elected leaders make consequential decisions based on a subset of annual government financial statements. These statements are supposed to present an accurate picture of financial health and activities, so that sound budgetary decisions can be made. But instead, these financial statements all too often don't give a complete and accurate account of what is going on. As a result, our leaders make bad decisions—knowingly or unknowingly—that come back to haunt and harm their constituents.

Nobody in this process is breaking the rules. **Indeed, the rules themselves are the source of deception—and they have become entrenched. The good news is that we have an opportunity to change them, but we must act urgently and with determination.**

The Problem and the Solution

The vast majority of state and local governments follow nationwide accounting standards set by a private-sector organization --the Government Accounting Standards Board (GASB). This board has seven members who are usually former government and/or credit rating agency employees, and who are often tied to special interests with a stake in government decisions and actions.

Among other things, GASB sets the accounting standards for local and state government “budgeted funds,” including the “general fund.” Why is that so important? Elected officials look at the general fund's financial report when developing their budgets. **If these financial statements don't present reality, then budget decisions are based on fiction.**

GASB's current standards for financial reports adhere to “modified accrual accounting” methodology. “Modified accrual accounting” is essentially a thinly disguised name for “cash basis accounting.” It is a far cry from the “full accrual” standard that Truth in Accounting supports and that insists on financial reality. Using modified accrual accounting, financial reports show expenses when money is paid, not when expenses are incurred.

For example, if a government promises to pay its workers a pension at some point in the future, those dollars don't appear as an expense in financial statements until the pension benefits are paid or when the government actually puts money into the pension plan. If a government takes out a loan, the loan proceeds are recorded as revenue, but the debt isn't shown as a liability in the budgeted funds.

So, using modified accrual accounting standards, these financial statements paint a much rosier, but far from accurate, picture of government finances by only reporting cash spending, and not the debt accumulated. It's as if you made your own spending decisions by looking only at how much is in your checking account now, while ignoring your growing outstanding credit card balance. It completely obfuscates governments' true financial condition.



This all might seem academic, but there are dire real-world consequences. As bills pile up, the ticking time bomb gets larger. When it comes time to pay, the bomb explodes. Suddenly, elected officials need to hike taxes or slash services—or both. **People suffer.** We’re already seeing this story play out in many states and municipalities across the country. In some states, contractors and nonprofits that provide services to the most-needy residents can’t get paid by the government in a timely manner.

As a result of the bad budgeting and accounting practices, New York went into the coronavirus pandemic in poor fiscal health. During these troubling times, 700 nonprofit organizations signed onto a letter to Governor Cuomo about how the decision to delay payments to nonprofits puts them at serious risk for financial failure. Services provided by these nonprofits include eviction assistance and housing support, drug and alcohol addiction treatment, child care and early learning, behavioral health, and housing support including affordable housing for the homeless.

In another example of the consequences of bad accounting, in early 2019, Texas officials touted a \$13 billion surplus in its general fund but that did not include \$75 billion of pension debt. Nevertheless, based on this “surplus,” within weeks the state’s final budget included increases in teacher salaries and property tax relief, leading to further deterioration of the state’s overall financial position. Whether you consider yourself liberal, conservative or moderate, we can all agree this is no way to run a government. Look around—what business could ever operate that way and stay afloat?

There is a simple, common-sense solution. GASB must adopt “**FACT-based accounting standards**” (FACT stands for “Full Accrual Calculations and Techniques”) for the budgeted funds. Adopting these standards would mean that the financial statements used for budgeting must

show expenses as they are incurred, especially when a government makes a promise to pay in the future. These are the same standards that most businesses, by law, must use in their financial reporting to the IRS. If government leaders demand FACT-based accounting when it comes to business finances, shouldn’t we expect them to apply those same standards to our governments’ finances?

If governments start using FACT, then the media, watchdog groups and the general public would all have a transparent look at how taxpayer dollars are being allocated. Elected officials would need to explain the actual implications of their budgetary decisions. As a society – and a democracy— we could finally have an honest debate about what we want our state and local governments to do for us—and how the bills will get paid.

We Have the Power to Make Common Sense Change

GASB has not made a fundamental change to funds accounting for decades. This is our opportunity to solve this problem once and for all.

GASB has essentially proposed maintaining the status quo, but we have the chance to change that by making our voices heard. Because GASB is a private entity, it isn’t directly accountable to voters. Even so, it must engage in a public, transparent process to consider input and make decisions. GASB is accepting public comments until February 26, 2021 on setting accounting standards for state and local governments. GASB will then hold five public hearings across the country in March and April (it is still to be determined if these will be live, virtual—or a mix of both). Generally, GASB and its work doesn’t draw much public scrutiny. Even though its decisions can affect the lives of hundreds of millions, GASB usually makes those decisions

behind a cloud of complex, arcane technical issues that have kept the public, the media and other stakeholders from playing a significant role in the process—or even being aware that it’s playing out.

It is vital that we act now. This time must be different. Truth in Accounting is mobilizing experts, advocacy organizations, watchdog groups, journalists and everyday citizens to let

GASB know that we’re watching and demanding that they institute common sense, FACT-based accounting standards. A sustained drumbeat of public comment between now and April 2021 will create momentum for change and hopefully lead to the necessary outcome. We urge you to join us in this effort.

Here’s how
you can make
your voice
heard by GASB:



Submit a public comment

Comments should be addressed to the Director of Research and Technical Activities, Project No. 3-25, and emailed to director@gasb.org. The deadline for comments is February 26, 2021, but **now** is the time to start showing support for FACT-based accounting!

To learn more, click on this link:

<http://www.truthinaccounting.org/resources/page/fact-based-accounting>

